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**SECTION 1**  
**INTRODUCTION TO LIBRARY FUND ACCOUNTING**

**A) PURPOSE**

The purpose of a library accounting system is (a) to show that all applicable legal provisions have been complied with; and (b) to represent fairly and accurately the financial position (Balance Sheet) and results of financial operations (Income Statement) of the library's funds and account groups.

**B) DEFINITION OF A FUND**

A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts recording cash and/or other resources together with all related liabilities, obligations, reserves and equities that are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with specific regulations, restrictions or limitations. Each fund is a completely separate accounting entity in itself, with its own accounts to record various transactions. Funds with similar characteristics are grouped together in fund groups.

**C) COMMENT**

While a private business enterprise can be viewed as a single economic entity with one group of assets, liabilities and equity accounts that are normally reflected in a single set of financial statements, a library may have several funds, each of which has its own assets, liabilities and fund equities. A library may be a combination of several distinctly different operations, each of which functions, and must be reported on, independently from any other fund (e.g. General Fund, Special Revenue Fund, etc.).

The implementation of GASB Statement 34 will add a layer of financial reporting in addition to the distinct fund reporting mentioned above. This new layer will consolidate the activity of governmental units into a single financial report, similar to the way private enterprise prepares financial reports. This new layer of financial reporting will be on the "full accrual" basis of accounting.

It is important to realize that the day-to-day recordkeeping will not change substantially. The recording of receipts and disbursements and the preparation of budgets for most libraries will continue to be maintained on the "modified accrual" basis of accounting.

Refer to Chapter 11 for a complete discussion of the requirements of GASB Statement 34.

**D) USERS OF LIBRARY FINANCIAL INFORMATION**

1. Taxpayers
2. State Treasurer/Oversight Bodies
3. Administrative/Finance
4. Bond Rating Agencies
5. Intergovernmental Grantors)
6. Contributors/Creditors
7. Employees (and their unions)

**SECTION 2  
BASIS OF ACCOUNTING**

There are two basic methods of accounting for funds: the modified-accrual basis and the accrual basis. Under the modified-accrual basis of accounting, revenue and expenditures are recorded as described below. Under the accrual basis of accounting, revenue is recorded when earned and expenses are recorded when incurred. In general, governmental libraries will utilize the modified-accrual basis of accounting in the day to day accounting records and budgets. When preparing the year end financial report, they will also prepare government wide financial statements on the full accrual basis of accounting.

**CHARACTERISTICS OF MODIFIED-ACCRUAL BASIS OF ACCOUNTING ARE AS FOLLOWS:**

- Expenditures are recorded when incurred (i.e., when the goods are received or the services rendered), not when cash is paid or when an invoice is received. Special rules are provided for the following:
  - **Prepaid expenses:** Purchases that benefit more than one period (such as insurance paid in advance) may be prorated (but typically are not) between periods.
  - **Interest on long-term debt** should be counted on the due date of the debt.
  - **Employee compensated absences** (e.g. sick and vacation pay) should be counted when the amount comes due for payment, i.e. time is taken off, or the employment is terminated (note: prior to the adoption of GASB 34, compensated absences are to be recognized if paid shortly after year end, generally within 60 days).
  - **Contingent liabilities** (e.g. lawsuits) should also be recorded at the time they come due for payment.
  - **Capital assets** should be counted as expenditures when purchased rather than capitalized and recognized over its useful life (i.e., depreciation).

- Revenue is recorded when collected or collectible soon enough to be used to pay current liabilities (referred to as “available”). “Available” generally means collectible within 30 to 60 days. Special rules are provided for the following:
  - **Property taxes** should be recorded in the fiscal period for which they were levied, provided the “available” criterion is met.
  - **Grants receivables** for reimbursement of expenditures should be counted at the same time that the expenditure is recorded, however, GASB Statement number 33 (effective in 2001) requires that the corresponding revenue be recorded using the “measurable and available” rules. When a grant receivable will not be collected until a date beyond the “available” criterion, a deferred revenue should be recorded.
  - **Miscellaneous revenue** such as fines and fees etc., are generally recognized when the cash is received.
  - **Proceeds of long-term debt** are recorded as an “other financing source” (similar to revenue), rather than as liabilities of the fund.

#### CHARACTERISTICS OF FULL ACCRUAL BASIS OF ACCOUNTING ARE AS FOLLOWS:

The full accrual basis is used to report the government wide financial information. After the accounting records of the individual funds have been completed on the modified accrual basis, then each government will also create government wide financial statements on the full accrual basis. This basis of accounting measures total economic resources, rather than just the current financial resources. As a result,

- Revenue is recorded when earned, regardless of when it is received.
- Expenses are recorded as soon as a liability is incurred, and are allocated to the periods benefited.

Some of the more significant differences from modified accrual includes:

- Property tax revenue is recorded in the period levied, less an allowance for uncollectible amounts (i.e., delinquent collections are recognized in the first year)
- Unused vacation time is recorded as an expense when it is earned
- Capital purchases are not recorded as an expense at the time of purchase; instead, depreciation expense is recorded over the estimated useful life of capital assets. This means that purchases of library books would be capitalized as an asset and depreciated over an appropriate time period.

### SECTION 3 TYPES OF FUNDS

Following is a list of the typical funds which may be found in accounting for governmental libraries:

#### **A) GENERAL FUND**

The General Fund accounts for all revenue and expenditures that are not required to be accounted for elsewhere. This fund typically accounts for the daily revenue and expenditures necessary to operate and provide service of a library. Most revenue and expenses are recorded in this fund. In many cases, this may be the only fund the library maintains.

#### **B) SPECIAL REVENUE FUNDS**

Special Revenue Funds are used to account for the proceeds of earmarked revenue or financing activities requiring separate accounting because of legal or regulatory provisions. In many cases, the use of the separate fund is mandatory. Typical special revenue activity might include accrued employee benefits (e.g. accumulated vested leave time) and LSTA grants. This could potentially include endowment type situations, where the principle of the gift may be spent to support the Library's programs.

#### **C) DEBT SERVICE FUNDS**

Debt Service Funds are used to account for the annual payment of principal, interest and expenses in connection with certain long-term debt. The proceeds from bond issues or other types of debt are typically recorded in the General or Capital Project Funds, depending on the stipulations of the debt instrument. Debt service fund resources are typically received via special voted property tax levies or transfers from other funds. In many cases, the use of Debt Service Funds is optional.

#### **D) CAPITAL PROJECTS FUNDS**

Capital Projects Funds are used to account for the development of capital facilities, such as an addition to a building. Typically, this fund is established to account for the construction of fixed assets or to set aside money for future capital needs. In many cases, the use of Capital Projects Funds is optional.

#### **E) ENDOWMENT FUNDS/PERMANENT FUNDS**

Prior to GASB Statement number 34, Endowment Funds were established to account for gifts and bequests that may be either expendable or nonexpendable, depending on legal restrictions that apply. While recording activity under a separate fund is common, it is not mandatory. In many instances, gifts and bequests may be accounted for under the General Fund.

GASB Statement number 34 created a new fund type called Permanent Funds that are used to report resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support the reporting government's programs. Permanent funds report trust arrangements in which the reporting government is the beneficiary, including public-purpose funds previously classified as nonexpendable trust funds.

**F) ACCOUNT GROUPS**

Prior to the implementation of GASB Statement number 34, in addition to the funds listed above, there are also two self-balancing account groups:

- **General Fixed Assets Account Group**

The General Fixed Assets Account Group is set up to account for long-lived assets. The assets are always acquired through a fund, usually the general fund or a capital project fund. The acquisition is accounted for as an expenditure and, therefore, no depreciation is applied against the asset. However, beyond the date of acquisition, the assets are accounted for in the general fixed assets account group. Essentially, the account group is a summary of all the long-lived assets.

When recording assets in this account group, consideration should be given to materiality and useful life of the item. Only material items need to be accounted for as fixed assets. Libraries should establish a dollar threshold for items to be capitalized. The objective is to establish a limit high enough to avoid too much detailed record keeping yet low enough to record material fixed assets. In the event the items are sold or retired, the cost of the item should be deleted from the account group.

Prior to GASB Statement number 34, books, periodicals, recordings and film were often recorded at one dollar per item. When GASB Statement 34 is implemented, assets including books, periodicals, recordings, etc should be reported at their historical cost, net of accumulated depreciation. Refer to Chapter 11 for a complete discussion. Replacement value is often estimated based on trade publication average costs adjusted for discounts and processing costs applicable to a library's purchases. Periodically, a library should compare its insurance coverage to replacement value.

- **General Long-term Debt Account Group**

The General Long-term Debt Account Group is set up to account for the unmatured principal of bonds, warrants, notes and other forms of long-term indebtedness that is secured by the full faith and credit of the library. The proceeds from issuing general long-term debt are recorded as revenue, typically in a capital projects fund or the general fund as "other financing sources." The debt service fund typically records the expenditure of the debt payments. However, beyond the date of issue, the outstanding principal amounts are accounted for in the general long-term debt account group. Essentially, the account group is a summary of all long-term debt owed by the library. As debt is retired, the account group is reduced.

Effective with the implementation of GASB Statement 34, reporting of the account groups will no longer be required, however, as discussed in the chapter on GASB Statement number 34, fixed assets and long term liabilities will be reported on the Statement of Net Assets. It will be necessary for each governmental unit to maintain the records regarding the historical cost of assets, along with the related accumulated depreciation expense and the long term debt. Although there are several alternatives to maintaining this information, libraries should consider continuing to track the information in a manner equivalent to the current techniques used for the General Fixed Asset Account Group and the General Long-term Debt Account Group, with the added emphasis on recognizing annual depreciation expense and accumulated depreciation.

## SECTION 4

### COMPARISON OF GOVERNMENTAL FUNDS AND COMMERCIAL ACCOUNTING

#### A) SIMILARITIES

- Periodic balance sheets or statements of net assets, income statements and statements of changes in equity balances are prepared by both. The double entry system of accounts is utilized by both.
- The historical cost principle (items are recorded based on their cost at the time of the transaction), consistency principle (using consistent accounting practices) and, for the most part, generally accepted accounting principles are used by both.
- Fund accounting and commercial accounting use the same accounting terminology. However, fund accounting has some terminology unique to it (e.g. fund balance instead of equity).

#### B) DIFFERENCES

- A profit motive is absent from all the funds. Libraries are service and responsibility oriented.
- Most libraries use a “modified-accrual” basis of accounting, where commercial accounting uses accrual basis. Under the requirements of GASB Statement number 34, the day-to-day recordkeeping will continue to be done on a modified accrual basis. The new statement will, however, add a layer of financial reporting to the current modified accrual basis of reporting. The new layer will bring together the financial information of the Library as a complete entity using the full accrual basis of reporting in a manner similar to most commercial accounting.
- The fund accounting emphasis is on “budgetary accounting.”
- In the fund level “modified-accrual basis” of accounting, capital expenditures are treated the same as operating expenses. Accordingly, governmental libraries typically do not compute depreciation expense at the fund level of financial reporting. This practice differs from commercial accounting where capital purchases are accounted for in asset accounts and charged to expense over time through the depreciation account.
- Some accounting systems record purchase orders on the books as encumbrances in the library funds. Generally accepted accounting principles do not record these as expenditures, however the accounting rules do allow encumbrances to be included in the comparison of actual results of operations to budget. Although not a common practice, encumbrance accounting may provide a superior form of budget control during the year.
- A library may be a combination of several distinctly different financial operations, each having its own set of accounts or funds.
- Governmental accounting is concerned more with a comparison of actual results to budgeted amounts, rather than a maximization of net income or working capital, as in commercial accounting.

## SECTION 5

### GOVERNMENTAL ACCOUNTING STANDARDS BOARD (GASB)

The GASB was established as an arm of the Financial Accounting Foundation in April 1984 to promulgate standards of financial accounting and reporting with respect to activities and transactions of state and local governmental entities. The GASB is the successor organization to the National Council on Governmental Accounting (NCGA).

GASB Concepts Statement 1 states: "Governmental financial reporting should provide information to assist users in (a) assessing accountability and (b) making economic, social and political decisions." In order to meet these overall objectives, GASB issued the following guidelines regarding financial reporting:

#### A) ACCOUNTABILITY

Financial reporting should assist in fulfilling government's duty to be publicly accountable and should enable users to assess that accountability. To accomplish this goal, financial reporting should meet the following criteria:

- Provide information to determine whether current year revenue was sufficient to pay for current year services.
- Demonstrate whether resources were obtained and used in accordance with the entity's legally adopted budget; it should also demonstrate compliance with other finance related legal or contractual requirements.
- Provide information to assist users in assessing the service efforts, costs and accomplishments of the governmental entity.

#### B) DECISION-MAKING

Financial reporting should assist users in evaluating the operating results of the governmental entity for the year. To accomplish this objective, financial reporting should also meet these criteria:

- Provide information about sources and uses of financial resources.
- Provide information about how the governmental entity financed its activities and met its cash requirements.
- Provide information necessary to determine whether the entity's financial position improved or deteriorated as a result of the year's operations.

## SECTION 6 MISCELLANEOUS ITEMS

### A) LIBRARY TYPES

There are a variety of library types and sizes. State laws governing how a library is established, levies taxes, issues and pays for debt, qualifies for state-funded revenue and performs other business functions vary depending on the type and size of a library. Refer to the Library Laws Handbook from the Library of Michigan, the State Laws Relating to Michigan Libraries, or consult legal counsel for detailed information concerning legal matters for the type and size of your library.

### B) USERS OF GOVERNMENTAL FINANCIAL STATEMENTS

The public is vitally concerned with the cost of public services, the adequacy of revenue in meeting such costs and the stewardship and efficiency of both elected and appointed officials. Contributors and bankers are also interested in the financial status and operating results. With the development of extensive and complex intergovernmental fiscal relationships in the form of grants-in-aid, shared revenue and administrative supervision, governments must be provided with adequate financial data on the operations of other governmental jurisdictions with which these relations exist. In addition, educational and research organizations, statistical reporting agencies and such individuals as accountants, financial analysts and economists whose professional activities embrace the study and improvement of financial administration and, of course, public management whose responsibility it is to evaluate past performance in daily decision-making and in planning future operations are also users.

### C) GRANTS

In recent years, many libraries have received grants and other revenue from various federal and state agencies. In connection with these, recipients agree to comply with various statutes and regulations that accompany the grants. The various statutes and regulations may vary among libraries, thus every library should follow its own agreement accordingly. Typically, most agreements are pass-through monies (i.e., federal money provided to large organizations which then provide grants to many organizations). These types of grants are usually reimbursement in nature and as expenditures are incurred, revenues are accrued. In addition, some statutes and regulations require that certified public accountants perform audits of libraries to test the compliance with these statutes and regulations in addition to performing financial audits (see Audit Process chapter).



**D) CHART OF ACCOUNTS**

A chart of accounts is an organized listing of all accounts used by a library to record financial information in its general ledger. The chart of accounts is to the accounting function what the Dewey Decimal System is to a library. It provides a foundation for arranging financial data into useful information. To provide reliable and consistent financial information, it is imperative that the chart of accounts be simple and functional. Accordingly, a "Uniform Chart of Accounts" has been developed by the State of Michigan under Public Act 2 of 1968, as amended, for all Michigan units of government. Information regarding the "Uniform Chart of Accounts" may be obtained by referring to Michigan Compiled Laws (MCL) 141 or from:

The State of Michigan  
Local Audit and Finance Division  
Department of Treasury  
Treasury Building  
Lansing, Michigan 48922  
(517) 373-3227  
[www.treas.state.mi.us](http://www.treas.state.mi.us) or  
[www.michigan.gov/treasury](http://www.michigan.gov/treasury)

**E) RECORD RETENTION**

Under MCL 399.5 and 750.491, government agencies must keep official books, papers or records unless it has received approval by filing a MH-38, Certificate of Records Disposal, with the State Archives of Michigan. However, a library may adopt its own record retention and disposal plan. Such individual plans must be approved by the State Archives of Michigan. Additional information may be obtained from:

State Archives of Michigan  
Michigan Department of State  
717 W. Allegan  
Lansing, Michigan 48918  
(517) 373-1408  
[www.sos.state.mi.us](http://www.sos.state.mi.us)

**F) TAX EXEMPT STATUS**

The General Sales Tax Act and Michigan Sales and Use Tax Administrative Rule, generally provides that governmental and not-for-profit library purchases are not subject to sales and use tax. Michigan Department of Treasury Revenue Administrative Bulletin 1996-6 illustrates the recommended sales and use tax exemption claim formats. Typically, a library will provide its vendors with a blanket certificate of exemption at the time of purchase. Additional information may be obtained from:

The State of Michigan  
Sales, Use and Withholding Taxes Division – Technical Section  
Treasury Building  
Lansing, Michigan 48922  
(517) 373-3190  
[www.treas.state.mi.us](http://www.treas.state.mi.us) or  
[www.michigan.gov/treasury](http://www.michigan.gov/treasury)

## G) SELECTION OF ACCOUNTING SOFTWARE

There are a number of factors to consider when selecting accounting software. This is true for both large and small library organizations. Key steps involved in selecting accounting software include the following:

- Assess Existing Resources – Determine current resources in terms of software, hardware and funding.
- Assess User Requirements – Survey individuals that will be using the software to determine needs/desires over the near-, medium- and long-term, volumes of transactions in the near- and long-term and expectations concerning the potential benefits to be gained from use of the software.
- Identify Available Software – Identify available software by surveying similar organizations, reading articles and software directories, attending trade shows or contacting consultants. Make an initial determination of potential vendors.
- Evaluate Vendors – For entry or mid-level “off-the-shelf” software packages, evaluation of vendors may be accomplished by identifying the perceived strengths and weaknesses of the different packages based on research conducted before making a final determination. For other software packages, a more formal selection process may be undertaken. This could include developing detailed software specifications, soliciting bids from potential qualified bidders, evaluating bid responses and attending vendor demonstrations prior to making a final determination. Factors to evaluate include, but are not limited to the following: ease of use; vendor knowledge, stability and support; flexibility; expandability; security; ability to track needed information and ability to access needed information.
- Implementation – Once software has been selected and purchased, a strategy should be developed for how to implement the software. Establish dates for accomplishing specific tasks. Regularly review progress of implementation. A rule-of-thumb is to run both the old and new systems (run parallel systems) for a month or two to ensure that a back up exists if problems occur with the new system. This is typically time-consuming and, therefore, should be taken into account when planning the implementation.